

Company Update report

VHC_Vinh Hoan Corporation

BSC

20/02/2020

NEGATIVE IMPACT OF SARS – CoV- 2

Recommendation Neutral

Nguyễn Thị Cẩm Tú (cơ bản)

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Target price	35,000
Current price	34,450
Upside	1.6%

Lê Quốc Trung (ptkt)

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Target price	N/A
Current price	N/A

Market Data

Outstanding share (mil)	183,376,956
Mkt Cap (VND. bil)	6,368
High of 52 w	56,150
Avg Vol 10 days (share)	159,571
Foreign ownership	34.50%

Major shareholders (%)

Trương Thị Lệ Khanh	42.88%
Mitsubishi Corporation	6.50%
Vietnam Investment Fund	4.98%
Norges Bank	2.63%
KB Vietnam Focus Balanced Fund	1.57%

Chart (1 year)



Company Overview: VHC is leading producer and exporter of Pangasius, supplying international customers with high – quality lines of products. Major exporting markets are USA, EU and China.

Valuation

We downgrade our recommendation from **BUY** to **NEUTRAL** to VHC stock and adjust the new target price to 35,000 VND/share due to (1) 2019 business results are much lower than expectation (2) BSC adjust the forecast for 2020 (taking into account the impact of the nCoV epidemic).

2020 Business Plan

In 2020, BSC forecasts VHC's net revenue and profit after tax reach VND 8,645 billion (+9.9% YoY) and VND 956 billion (-18.9% YoY) (lower 23.0% and 38.4% respectively compared to the previous forecast). 2020 EPS is forecast at 5,197 VND/share, equivalent to PE fw 2020 of 6.6.

Investment Risks

+ Affected by the nCoV epidemic, consumption in the Chinese market is expected to decrease in the following quarter

+ Higher competition in US market in case of POR 15 official of 0% (preliminary POR15 is 0%)

Business update

2019 business results plummeted. VHC's revenue and profit after tax reached VND 7,867 billion (-15.14% YoY) and VND 1,180.4 billion (-18.16% YoY) respectively, equivalent to completing 78.3% of the revenue plan and 94.0% of the plan PBT. This result is much lower than the latest forecast of BSC: lowering than 12.9% and 11.2% respectively. Accumulated 11M.2019, exports reached US 296 million (-12.4% YoY).

BSC thinks that even 2019 business result was at low level, it is difficult to create strong growth for 2020 when the demand in major markets has not shown signs of improvement.

The impact of the nCoV epidemic will have a strong impact on the Chinese consumption in Q1.2020. Thus, China, the main growth driver of pangasius industry, is negative in the short term.

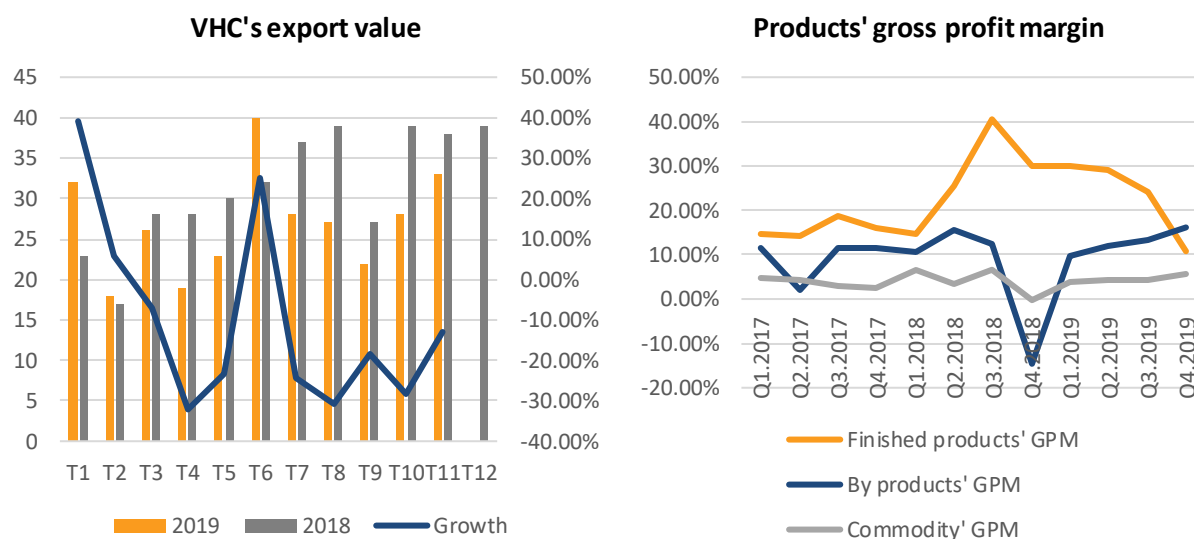
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The difference in BSC's forecast and actual results is mainly due to (1) Export value of the industry (especially in 2H.2019) has recorded a deeper decline than BSC's forecast; (2) Gross profit margin is much lower than our expectation.

- (1) **The decrease in value of major exporting markets was much worse than our expectation.** By 2019, the industry's export value to USA reached USD 270.5 million (-48.5% YoY), EU market reached USD 225.9 million (-2.3% YoY) while Chinese market reached USD 619.6 million (+22.7% YoY). Market prices also plunged from the peak: the average selling price in USA and China in 2019 reached USD 3.55/kg (-36.06% YTD) and USD 2.08/kg (-23.80% YTD). BSC comments that the disappointing exporting value in USA market was due to (1) the high inventory level lasted longer than expected (2) the decrease in raw pangasius prices in the domestic market reduced the selling prices.

Due to the fact that USA market accounts for 68% of the export value of VHC in 1H.2019 (BSC assumes this proportion does not change in the whole of 2019), Vinh Hoan is directly affected by the worsening business environment. Accumulated 11M.2019, the company's export value reached US \$ 296 million (-12.4% YoY).

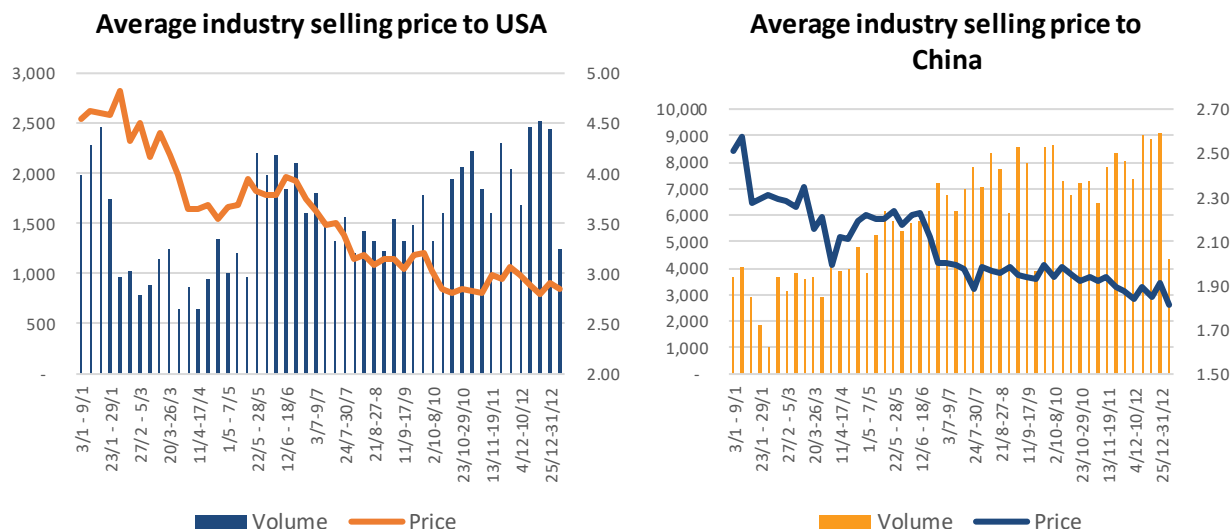


Source: VHC

- (2) **Gross profit margin of products is lower than our forecast.** For pangasius fillet products, the negative fluctuations of export prices and raw material prices (especially in 2H.2019) caused the sharp decline in VHC's gross profit margin which reached in four consecutive quarter of 2019: 29.87%, 28.98%, 23.95% and 10.77%. BSC believes that margin in P&L statement is lagged by 1 quarter compared to the actual gap between material prices and selling prices, mainly because the contracts are usually signed in

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advance. Meanwhile, Collagen and Genlatin - the BSC segment expected to make up for the decrease of fillet segment did not turn out a good result.



Source: BSC Research

2020 Business outlook and BSC forecast

Prospects for pangasius industry in 2020: BSC believes that despite low – level in 2019, it is still difficult to create a sudden growth for 2020 when the demand in main markets has not shown signs of improvement. Two major markets (US and EU) currently have not shown any recovery of demand, however, BSC expects export value will be more positive in 2H.2020 when (1) inventories fall (2) Demand increases due to the seasonal reason. For Chinese market, the impact of SARS – CoV - 2 epidemic will have greatly negative impact on consumption on Q1.2020. Thus, China - the main growth driver of pangasius industry – has difficulties in the short term, making the industry prospect less optimistic.

The impact of SARS – CoV - 2 on the pangasius industry: Exporting to China - Hong Kong market in 2019 reached USD 662.5 million (+25.3% YoY), accounting for 33% of total export value in Vietnam. The outbreak of SARS – CoV - 2 in China since January 2020 will have negative impact on Vietnam pangasius industry. BSC believes that in Q1.2020, pangasius exports to China will decline sharply in both volume and value, before bouncing back in Q2.2020.

- (a) Demand will weaken due to Chinese people extending the holiday season, limiting recreational activities and eating out. Therefore, supermarkets, restaurants and schools - the main distribution channels of pangasius will record a sharp decrease.
- (b) Tightening customs clearance to prevent the outbreak of SARS – CoV - 2 also slows down the flow of goods. However, BSC believes that the tightening will not have a lasting effect.
- (c) With the fact that Chinese market accounts for 15% of VHC's exporting value, the reduction in demand in China market will directly impact on Q1.2020 results. VHC said that the company has reduced its planned profit in 2020 by 10% compared to the original plan, and transferred the capacity which initially exported to China to EU market to reduce the impact of the disease.

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BSC 's 2020 business forecast

In 2020, BSC forecasts that VHC's net revenue and profit after tax will be respectively VND 8,645 billion (+ 9.9% YoY) and VND 956 billion (-18.9% YoY) based on the following assumptions:

+ Revenue breakdown: Pangasius fillets revenue is expected of VND 6,189 billion (+ 8.6% YoY), accounting for 71.6% of total revenue. Merchandise sales reached VND 1,441 billion (+ 23.9% YoY) and by-products revenue reached VND 960 billion (-0.7% YoY).

+ Price and volume: output + 10% YoY (BSC expects after the SARS – CoV - 2 epidemic is controlled, the demand increases in China), prices -2% YoY.

+ Gross profit margin in 2020 is forecast to reach 16.9%, down from 19.4% in 2019. BSC expects VHC's gross profit margin to sharply narrow because (1) the selling price is expected to decrease by 2% YoY and (2) material costs are expected to increase by 9% from the current level.

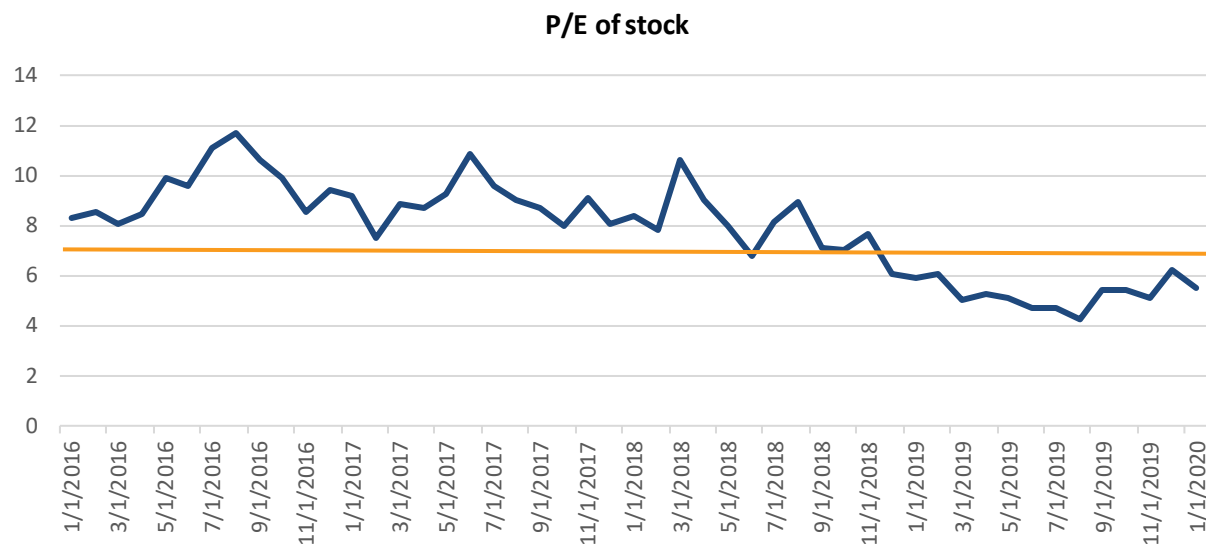
+ SG&A expense margin in 2020 is 5% of net revenue (same as 2019).

Business Forecast Table

Unit: VND bill	2018	2019	2020F	2020F mới
Net revenue	9,271	7,867	11,233	8,643
<i>Growth</i>	13.7%	-15.1%	42.8%	9.8%
Finished product revenue	7,366	5,699	8,881	6,189
By – product revenue	1,102	967	1,416	960
Merchandise revenue	864	1,163	936	1,441
Raw material's revenue	21	9	47	47
Service revenue	53	55	6	5
Cost of goods sold	(7,232)	(6,334)	(8,919)	(7,183)
Gross profit	2,039	1,533	2,314	1,461
<i>Gross margin</i>	21.9%	19.4%	20.6%	16.9%
Selling expense	(210)	(252)	(247)	(268)
<i>Selling expense margin</i>	2.2%	3.2%	2.2%	3.1%
Administration expense	(144)	(149)	(181)	(133)
<i>Administration expense margin</i>	1.5%	1.8%	1.6%	1.7%
Profit before tax	1,688	1,309	1,826	1,125
Profit after tax	1,442	1,180	1,552	956
EPS	15,489	12,573	8,376	5,197
<i>Growth</i>	137.9%	-18.8%		

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+ PE valuation: Currently, VHC's stock price is trading around P/E trailing = 5.5. BSC still holds the target P/E of 5.5 as in the previous report to determine the stock value after adjusting the business results forecasts in the coming years.



Source: Bloomberg

PE Valuation	2020	2021	2022
EPS	5,197	5,455	7,110
PE	5.5	5.5	5.5
Value of a share	28,600	30,000	39,100

+ FCFF Valuation:

	2020	2021	2022
Free cash flow to firm	338	590	740
Present value	294	463	489
Total firm value	8,293		
Debt	866		
Equity value	7,427		
No. of shares	183,376,956		
Value of a share (VND)	40,500		

WACC	
Rf	6%
Beta	0.9
Ke	13.83%
Kd	8%
E/A	60%
Tax rate	20%
WACC	10.86%
g	1%

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	Price	Proportion	Average price
FCFF	41,500	50%	20,750
P/E	28,600	50%	14,300
Target price			35,050
Current price			34,450
Upside			1.74%

We downgrade our **BUY** recommendation to **NEUTRAL** for VHC stock after revising our business results for the coming years. We adjust the target price for the stock from VND 46,700 (after dividend) to VND 35,000/share using P/E and FCFF methods with the proportion of 50% / 50%.

Disclosure

The information, statements, forecasts and projections contained herein, including any expression of opinion, are based upon sources believed to be reliable but their accuracy completeness or correctness are not guaranteed. Expressions of opinion herein were arrived at after due and careful consideration and they were based upon the best information then known to us, and in our opinion are fair and reasonable in the circumstances prevailing at the time. Expressions of opinion contained herein are subject to change without notice. This document is not, and should not be construed as, an offer or the solicitation of an offer to buy or sell any securities. BSC and other companies in the BSC and/or their officers, directors and employees may have positions and may affect transactions in securities of companies mentioned herein and may also perform or seek to perform investment banking services for these companies. This document is for private circulation only and is not for publication in the press or elsewhere. BSC accepts no liability whatsoever for any direct or consequential loss arising from any use of this or its content. The use of any information, statements forecasts and projections contained herein shall be at the sole discretion and risk of the user. No part of this material may be (i) copied, photocopied or duplicated in any form by any mean or (ii) redistributed without the prior written consent of BIDV Securities Company (BSC).

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